Internal Revenue Service

memorandum

CC:TL-N-5129-91
Br2:CTSanderson

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to: District Counsel, Washington CC:WAS
Attn: Wilton A. Baker, Special Litigation Assistant

from: Assistant Chief Counsel (Tax Litigation) CC:TL

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subject: [redacted] and [redacted]

On February 11, 1991, we received a copy of your memorandum to the Large Case Program Manager notifying him of a dispute that had arisen in a Rule 155 computation in the above consolidated cases. After coordinating with the appropriate branches in Tax Litigation and Technical, we subsequently provided oral advice to you on this matter. This memorandum is to confirm such advice.

ISSUES

1. Whether the Service should object to the Rule 155 computations proposed by petitioners on the ground that the proposed computations raise new issues.

2. Whether, if the court allows petitioners to raise these new issues, the Service should request leave to amend its pleadings to assert that the [redacted] should have included in its [redacted] taxable income $[redacted] of FDIC assistance provided to [redacted] immediately prior to the acquisition of [redacted] by [redacted] on [redacted].

3. Whether the statute of limitations is still open for [redacted]'s short taxable year ended [redacted], the date of [redacted]'s acquisition by [redacted].

CONCLUSIONS

1. Yes. The Service should object to the petitioners' contention in the Rule 155 computations that it is entitled to a refund of tax for [redacted], [redacted], and [redacted] as a result of the carryback of a net operating loss generated in [redacted]. The ground for the objection should be Tax Court Rule 155(c)'s provision that in a Rule 155 computation "no argument will be heard upon or consideration given . . . to any new issues."

2. No. Service position is clear that the FDIC assistance at issue was income to [redacted] for its short taxable year ended [redacted], not income to [redacted] for its taxable year ended [redacted]. We are aware of no legal basis for arguing that the assistance should be included in [redacted]'s income for its [redacted] taxable year.

3. No. [redacted] filed a return for a short taxable year ended [redacted]. This return did not include the first five days of [redacted] although [redacted] was still in existence as a separate entity for those days. However, the [redacted] return for [redacted], who acquired [redacted] on [redacted], did include items of [redacted] for the first five days of [redacted] and for the remainder of [redacted]. Accordingly, the statute of limitations for [redacted]'s short taxable year ended [redacted], began running on the filing of [redacted]'s [redacted] return, which was on [redacted]. This statute of limitations period was not suspended, however, by the notice of deficiency issued with respect to [redacted]'s [redacted] year; thus, [redacted]'s statute of limitations period for its short taxable year ended [redacted], is now closed.

FACTS

[redacted], the subject of [redacted], and [redacted], the subject of [redacted], are related entities whose cases were consolidated for trial before the Tax Court. On [redacted], and [redacted], the Tax Court issued opinions in the consolidated cases adverse to the Service. These opinions are reported at [redacted] and [redacted], respectively.

On [redacted], you filed T.C. Rule 155 computations and proposed decisions for the above cases. The computations and proposed decisions reflect that, under T.C. Rule 155, there is no deficiency due from, nor overpayment due to, petitioners for the years in issue. On [redacted], the petitioners filed a notice of objection to your Rule 155 computations and offered alternative computations. The petitioners contend in their alternative computations that petitioners are entitled to a refund as a result of a net operating loss generated in [redacted]. The petitioners did not raise the refund claim or the NOL issue in their pleadings or during trial.

Further relevant facts are as follows. In [redacted], the FDIC solicited bids for the acquisition of [redacted], a failed financial institution. The FDIC accepted a bid submitted by [redacted]. The FDIC agreed to make a $[redacted] contribution to [redacted] as part of the acquisition. Hence, on [redacted], the FDIC contributed such money to [redacted]. Following that payment, [redacted] was converted from a mutual savings bank into a state

chartered stock bank and renamed [redacted]. Then, also on [redacted] [redacted] acquired [redacted].

It is the Service's position that the $[redacted] FDIC assistance is taxable income to [redacted] for its short taxable year ended [redacted]. [redacted] did not include the assistance in income in its last return, which erroneously covered only the period ended [redacted], instead of the period ended [redacted]. The Service has never issued a notice covering [redacted]'s short taxable year ended [redacted] and such year is not before the court in this proceeding. However, the taxability of the FDIC assistance received by [redacted] was indirectly at issue in the tried cases because the character of the FDIC assistance (i.e., taxable income or nonshareholder contribution to capital) could have an effect on the basis of [redacted]'s assets. The court did not have to decide the issue, however.

DISCUSSION

Issue 1

As discussed in the telephone conference of [redacted], you should object to petitioners' claim for refund for [redacted], [redacted], and [redacted] on the ground that it is a new issue. Tax Court Rule 155(c) provides that in a Rule 155 computation "no argument will be heard upon or consideration given . . . to any new issues." The petitioners did not raise the claim for refund or the NOL issue in their pleadings or during the trial; accordingly, the allegation that petitioners are entitled to a refund on the basis of a [redacted] NOL is a new issue before the court, and the Service should object to it being raised in the Rule 155 computations.

Issue 2

Service position is clear that the FDIC assistance at issue is income to [redacted] for its short taxable year ended [redacted], not income to [redacted] for its taxable year ended [redacted]. This is true even though [redacted]'s last return did not include the assistance or any other items from the first five days of [redacted] and even though [redacted]'s consolidated return for [redacted] erroneously included [redacted] items from the first five days of [redacted]. We considered whether there are any mitigation or estoppel arguments for requiring [redacted] to include the assistance in its [redacted] return and concluded that there is no legal basis for making such an argument.

An additional reason for not raising the issue in this particular case is that dicta in the [redacted] case indicates that at least Judge [redacted] is already of the view that FDIC assistance such as that received by [redacted] is not taxable

income, but is instead a nonshareholder contribution to capital. See [redacted].

Issue 3

As stated above, [redacted]'s last tax return did not include the first five days of [redacted] as it should have. Therefore, the statute of limitations for [redacted]'s taxable year ended [redacted], would at first glance appear to be open as if no return was filed, under the authority of Gensinger v. Commissioner, 18 T.C. 122 (1952).

In Gensinger, the taxpayer filed a return for the period January 1, 1943, to July 7, 1943; however, the correct taxable period was the calendar year 1943. The Tax Court held that the return filed was "not the return required by law and did not serve to start the running of the statutory period for assessment and collection of any tax for the calendar year 1943." Gensinger, supra at 133. In other words, it was as if no return was filed for calendar year 1943.

In the present case, [redacted]'s last return was not the "return required by law" since it did include the first five days of [redacted]. However, [redacted]'s consolidated return for its taxable year ended [redacted], included [redacted], the successor to [redacted], for the period after [redacted] acquired [redacted] on [redacted]. [redacted]'s [redacted] return also erroneously included [redacted] items from the first five days of [redacted]. Although it did not arise in the consolidated return context, the Tax Court considered an issue similar to this in Atlas Oil and Refining Corporation v. Commissioner, 22 T.C. 552 (1954), acq., O.M. 10585.

In Atlas Oil, supra, the petitioner maintained its books of account on the basis of a calendar year. The petitioner did not file any returns for the calendar years 1942 and 1943, the years at issue before the court. However, the petitioner did file returns covering fiscal years ended November 30, 1942, November 30, 1943, and November 30, 1944, although a fiscal year filing by the petitioner was erroneous since it kept its books on a calendar year basis. The Service first issued notices for fiscal years November 30, 1942, and November 30, 1943, and such notices were petitioned by the taxpayer. The Tax Court concluded that there were no deficiencies in tax for these fiscal years since "the deficiencies were incorrectly determined on a fiscal year basis." Atlas Oil and Refining Corporation v. Commissioner, 17 T.C. 733, 740 (1952). Subsequent to that opinion, on March 28, 1952, the Service sent to petitioner notices of deficiency for the calendar years 1942 and 1943. The petitioner challenged these notices as being issued beyond the statute of limitations.

The Tax Court relied on the Board of Tax Appeals' holdings under similar facts in Mabel Elevator Co., 2 B.T.A. 517 (1925), and Paso Robles Mercantile Co., 12 B.T.A. 750 (1928), in concluding that the statute of limitations for calendar years 1942 and 1943 began to run on the filing of the returns for the fiscal years ended November 30, 1943, and November 30, 1944, respectively.

In rejecting respondent's "no return" argument, which was based on Gensinger cited above, the court stated the rationale of Mabel Elevator, Paso Robles, and other similar cases as follows:

> [W]hen the Commissioner is given information in properly executed form covering all of the period in issue the statute of limitations begins to run, even though the taxpayer may have mistakenly filed returns for improper periods. The cases are decided on the theory that the improper returns pieced together provide the Commissioner with the information necessary to determine the true tax liability of the taxpayer within the period provided by law. That rationale is incompatible with an argument such as the one advanced by respondent that since the return was not the one required by law, "no return" was filed and the statute of limitations never began to run.

Based on the above cases and rationale, the statute of limitations for [redacted]'s taxable year ended [redacted], began running on [redacted], the date that [redacted]s consolidated return for [redacted] was filed. At that time, the Commissioner was provided information necessary to determine the tax liability of [redacted] for its taxable year ended [redacted]. Any doubt that the above rule would apply in the consolidated context under the present facts is resolved by Treas. Reg. § 1.1502-75(g)(1), which provides:

> (g) Computing periods of limitation-(1) Income incorrectly included in consolidated return. If -
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> (i) A consolidated return is filed by a group for the taxable year, and
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> (ii) The tax liability of a corporation whose income is included in such return must be computed on the basis of a separate return (or on the basis of a consolidated return with another group),
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> then for the purpose of computing any period of limitation with respect to such separate return (or such other consolidated return), the filing of such consolidated return by the group shall be considered as the making of a return by such corporation.

Furthermore, although the statute for [redacted]'s short [redacted] year began running on [redacted], the date of the filing of [redacted]'s [redacted] return, it was not suspended by the issuance of the notice of deficiency for [redacted]'s [redacted] year or the filing of [redacted]'s petition for such year. This conclusion is also based on Atlas Oil, 22 T.C. 552. In Atlas Oil, the Service argued in the alternative that the prior fiscal year notices suspended the running of the statute of limitations for calendar years 1942 and 1943. The court rejected this argument as follows:

> The essence of the holding in the prior [Atlas] case is that this Court was without authority to consider the correctness or incorrectness of any proposed deficiency with respect to the fiscal years because deficiencies could be determined only on a calendar year basis. And since the deficiency notices were predicated on a fiscal year basis, this Court had no power to consider any possible deficiencies for the calendar years which overlapped or were comprehended within the fiscal years. The jurisdiction of this Court is limited by statute to consideration of the taxable years covered by the notice of deficiency . . . and we have made it plain that such jurisdiction does not embrace any periods other than the precise ones for which the Commissioner determined deficiencies. Estate of Cyrus H.K. Curtis, 36 B.T.A. 899, 903; cf. Linen Thread Co., Ltd., 14 T.C. 725, 731. Accordingly, this Court was without authority in the prior proceedings to approve deficiencies either for the fiscal years or for the calendar years.
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> It is basic, however, that the statute of limitations was suspended by section 277 [predecessor of section 6503(a)] only for such taxable years as were properly before the Court in prior proceedings. Similarly the Commissioner was prohibited by section 272(f) [predecessor of section 6212(c)] only from mailing further notices of deficiency "in respect of the same taxable years[s]" that were involved in the prior action. There can be no question that a taxable year ended November 30 is different from a taxable year ended December 31. . . . In the circumstances of such clear statutory distinctions between fiscal years and calendar years we can only conclude that the statute of limitations for the calendar years 1942 and 1943 was not tolled by the filing of the petitions to this Court contesting deficiencies determined for the fiscal years ended November 30, 1942, and November 30, 1943. And similarly we think that the Commissioner was not prevented by section 272(f) from asserting deficiencies

in taxes against this taxpayer for the calendar years 1942 and 1943.

Similar to Atlas, there is a clear distinction between [redacted]'s [redacted] taxable year and [redacted]s short taxable year ended [redacted]. There was nothing that prevented the Service from issuing a statutory notice of deficiency for [redacted]s short year prior to the expiration of the statute of limitations for such year. We see no basis for distinguishing the above holding in Atlas from the facts of the present case.

Accordingly, the issuance of the notice and the filing of the petition with respect to [redacted]'s [redacted] year did not toll the statute of limitations for [redacted]s taxable year ended [redacted]; such statute of limitations expired on [redacted], three years after the filing of the [redacted] return.

If you have any questions, contact Ted Sanderson on 566-3520.

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